THE UNIVERSITY OF TENNESSEE
KNOXVILLE, TENNESSEE

FOR THE YEAR ENDED
JUNE 30, 1996

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March 17, 1997

The Honorable Don Sundquist, Governor
and
Members of the General Assembly
State Capitol
Nashville, Tennessee 37243
and
The Honorable William B. Sansom, Chairman
Finance Committee
Board of Trustees
The University of Tennessee
Knoxville, Tennessee 37996-0180
and
Dr. Joseph Johnson, President
The University of Tennessee
831 Andy Holt Tower
Knoxville, Tennessee 37996-0180

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the University of Tennessee for the year ended June 30, 1996. You will note from the independent auditor's report that a qualified opinion was given on the fairness of the presentation of the financial statements. The university has elected not to record the liability for accrued compensated absences in its financial statements. In our opinion, accrued compensated absences should be recorded to conform with generally accepted accounting principles.

Consideration of the internal control structure and tests of compliance disclosed certain deficiencies, which are detailed in the Results of the Audit section of this report. The university's administration has responded to the audit findings; the responses are included following each finding. The Division of State Audit will follow up the audit to examine the application of the procedures instituted because of the audit findings.

Very truly yours,

W. R. Snodgrass
Comptroller of the Treasury

WRS/sdr
96/146

State of Tennessee

Audit Highlights

Comptroller of the Treasury | Division of State Audit

Financial and Compliance Audit
The University of Tennessee
For the Year Ended June 30, 1996

AUDIT OBJECTIVES

The objectives of the audit were to consider the university's internal control structure; to determine compliance with laws, regulations, contracts, and grants; to determine the fairness of the presentation of the financial statements; and to recommend appropriate actions to correct any deficiencies.

INTERNAL CONTROL FINDINGS

Inadequate Data Processing Security*
Computer users with high-level system access were not required by the security system to change their passwords regularly. Also, certain generic dataset profiles appear to have excessive access (page 9).

Inadequate Program Change Procedures
The University of Tennessee was not requiring adequate documentation for program changes within its computerized system (page 10).

COMPLIANCE FINDING

Failure to Promptly Return Financial Aid Refunds**
The University of Tennessee, Knoxville, did not always follow federal regulations for timely crediting of refunds to student financial aid programs (page 11).

* This finding is repeated from the prior audit.
** This finding is repeated from prior audits.

OPINION ON THE FINANCIAL STATEMENTS

The opinion on the financial statements is qualified because of the omission of the liability for accrued compensated absences from the financial statements.

“Audit Highlights” is a summary of the audit report. To obtain the complete audit report which contains all findings, recommendations, and management comments, please contact

Comptroller of the Treasury, Division of State Audit
1500 James K. Polk Building, Nashville, TN 37243-0264
(615) 741-3697

AUDIT REPORT
THE UNIVERSITY OF TENNESSEE
FOR THE YEAR ENDED JUNE 30, 1996

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THE UNIVERSITY OF TENNESSEE
FOR THE YEAR ENDED JUNE 30, 1996

INTRODUCTION

POST-AUDIT AUTHORITY

This is a report on the financial and compliance audit of the University of Tennessee. The audit was conducted pursuant to Section 4-3-304, *Tennessee Code Annotated*, which authorizes the Department of Audit to "perform currently a post-audit of all accounts and other financial records of the state government, and of any department, institution, office, or agency thereof in accordance with generally accepted auditing standards and in accordance with such procedures as may be established by the comptroller."

Section 8-4-109, *Tennessee Code Annotated*, authorizes the Comptroller of the Treasury to audit any books and records of any state governmental entity that handles public funds when the Comptroller considers an audit to be necessary or appropriate.

OBJECTIVES OF THE AUDIT

The objectives of the audit were

1. to consider the university's internal control structure to determine auditing procedures for the purpose of expressing an opinion on the financial statements;

2. to determine compliance with laws, regulations, contracts, and grants;

3. to determine the fairness of the presentation of the financial statements; and

4. to recommend appropriate actions to correct any deficiencies.

Although this audit was not intended to serve as an organization-wide audit as described in the Single Audit Act of 1984 and Office of Management and Budget (OMB) Circular A-128, "Audits of State and Local Governments," it included tests of compliance with applicable federal laws and regulations and consideration of the internal control structure used in administering federal financial assistance programs. This audit is a segment of the organization-wide audit of the State of Tennessee, which is conducted in accordance with the Single Audit Act of 1984 and OMB Circular A-128.

SCOPE OF THE AUDIT

The audit was limited to the period July 1, 1995, through June 30, 1996, and was conducted in accordance with generally accepted government auditing standards. Financial statements are presented for the year ended June 30, 1996, and for comparative purposes, the year ended June 30, 1995. The University of Tennessee has been included as a component unit in the *Tennessee Comprehensive Annual Financial Report.*

BACKGROUND AND ORGANIZATION

BACKGROUND

The University of Tennessee was first established as Blount College in 1794 by the legislature of the Federal Territory. In 1807, the legislature renamed the institution East Tennessee College and in 1840 designated it a university. East Tennessee University was selected by the state legislature to be Tennessee's land-grant institution under the terms of the Morrill Act of 1862. In 1879, the legislature chose the school to be Tennessee's state university and changed the name to the University of Tennessee.

Since its establishment, the university has grown into an institution with 23 different colleges and schools. With its primary campuses, various experiment stations, and extension services, the university provides services throughout the state. The main campus is in Knoxville; other campuses are in Memphis, Martin, and Chattanooga.

ORGANIZATION

The University of Tennessee is governed by the University of Tennessee Board of Trustees. In 1968, the board reorganized the institution into a university system, giving a central administrative staff the responsibility for the entire operation of the university and establishing on the primary campuses chancellors who are responsible for their respective campuses.

PRIOR AUDIT FINDINGS

Section 8-4-109, *Tennessee Code Annotated*, requires that each state department, agency, or institution report to the Comptroller of the Treasury the action taken to implement the recommendations in the prior audit report. The university filed its report with the Department of

Audit on June 4, 1996. A follow-up of all prior audit findings was conducted as part of the current audit.

RESOLVED AUDIT FINDINGS

The current audit disclosed that the university has corrected previous audit findings concerning the Central Services Accounting System at the University of Tennessee, Knoxville, and Title IV repayment policies at the University of Tennessee at Martin.

REPEATED AUDIT FINDINGS

The current audit disclosed that the university had not totally corrected the previous audit finding regarding refund procedures at the University of Tennessee, Knoxville. As was the case in the last two years, refunds were not returned to lenders or credited to the appropriate programs in a timely manner.

In addition, the previous audit finding regarding data security had not been corrected. Computer users with high-level system access were not changing their passwords on a regular basis.

OBSERVATIONS AND COMMENTS

In May 1996, the University of Tennessee's Audit and Management Services Division released a report on their special review of the university's marching band. The report revealed that the band director had misappropriated approximately $54,000. The majority of this loss was from the mishandling of meal money for out-of-town band trips. In addition, the band's clerk and secretary misappropriated approximately $1,200 and $1,500, respectively.

Numerous discrepancies related to the marching band's activities were discussed in the report. The improprieties over travel included the following: non-traveling students' names were added to meal per diem lists, portions of meal per diems were improperly retained, improper personal travel expenses were submitted, and false mileage claims were submitted. Proceeds from band tape sales were not properly handled. Funds in an unauthorized alumni band bank account were not properly accounted for. Irregularities were noted in the handling of a photographer's rebate. In addition, improper use of university supplies, personnel, and resources, as well as personal long distance phone calls, were noted.

In March 1996, the band director resigned from his administrative and tenured faculty positions at the university in lieu of termination. He waived his tenured faculty due-process rights, forfeited his unpaid annual leave, and agreed to pay the university the total loss determined by the audit. The university has accepted a plan for the director to repay $54,000. The clerk and the secretary repaid the questioned amounts, and their employment with the university was terminated in May 1996.

In December 1996, a follow-up internal audit report was issued on the activities of the marching band from 1980 through 1993. This report identified approximately $9,600 in discrepancies involving travel expenses, photographer commissions, and a music festival operated by the band's former director. The former director, who is retired, voluntarily repaid the amounts questioned in the internal audit report. He stated that he was not aware of certain approval requirements and that if this had been brought to his attention when it first occurred, he would have corrected that matter at that time. He further stated that because of the large number of band members, the many meals involved, and the time period covered during the review, he could neither verify nor dispute the discrepancies.

The matters above were both referred to the District Attorney General of the Sixth Judicial District (Knox County). The band director pleaded guilty in Knox County Criminal Court and received three years' probation and was required to make full restitution. The District Attorney's Office did not find it necessary to take action against the former director, who had repaid amounts in question.

The university has taken steps to correct the internal control deficiencies which contributed to these situations. During future audits we will review those steps as appropriate.

RESULTS OF THE AUDIT

AUDIT CONCLUSIONS

Internal Control Structure

As part of the audit of the university's financial statements for the year ended June 30, 1996, we considered the internal control structure to determine auditing procedures for the purpose of expressing an opinion on the financial statements, as required by generally accepted government auditing standards. The report on the internal control structure is on the following pages. Reportable conditions, along with recommendations and management's responses, are detailed in the findings and recommendations, which follow the report on the internal control structure. Consideration of the internal control structure disclosed no material weaknesses.

Compliance with Laws and Regulations

The results of our tests disclosed no instances of noncompliance that are required to be reported herein under generally accepted government auditing standards. Immaterial instances of noncompliance, along with recommendations and management's responses, are included in the findings and recommendations. The compliance report follows the findings and recommendations.

Fairness of Financial Statement Presentation

The university has elected not to accrue the liability for compensated absences. Since this accounting practice is contrary to generally accepted accounting principles, the Division of State Audit has rendered a qualified opinion on the university's financial statements. The independent auditor's report follows the compliance report.

Report on the Internal Control Structure Based on an Audit of the Financial Statements Performed in Accordance With *Government Auditing Standards*

September 20, 1996

The Honorable W. R. Snodgrass
Comptroller of the Treasury
State Capitol
Nashville, Tennessee 37243

Dear Mr. Snodgrass:

We have audited the financial statements of the University of Tennessee, a component unit of the State of Tennessee, as of and for the year ended June 30, 1996, and have issued our report thereon dated September 20, 1996. Our report was qualified because the university excluded the liability for accrued compensated absences from the balance sheet.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

The university's management is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles. Because of inherent limitations in any internal control structure, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the structure to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the effectiveness of the design and operation of policies and procedures may deteriorate.

In planning and performing our audit of the university's financial statements for the year ended June 30, 1996, we obtained an understanding of the internal control structure. With respect to the internal control structure, we obtained an understanding of the design of relevant policies and procedures and whether they have been placed in operation, and we assessed control risk in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide an opinion on the internal control structure. Accordingly, we do not express such an opinion.

We noted certain matters involving the internal control structure and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the university's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements.

The following reportable conditions were noted:

- Data processing security was not adequate.
- Program change procedures were not adequate.

These conditions are described in the Findings and Recommendations section of this report.

A material weakness is a reportable condition in which the design or operation of one or more of the specific internal control structure elements does not reduce to a relatively low level the risk that errors or irregularities in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Our consideration of the internal control structure would not necessarily disclose all matters in the internal control structure that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. However, we believe none of the reportable conditions described above are material weaknesses.

We also noted other matters involving the internal control structure and its operation that we have reported to the university's management in a separate letter.

This report is intended for the information of the General Assembly of the State of Tennessee, the board of trustees, and management. However, this report is a matter of public record, and its distribution is not limited.

Sincerely,

Arthur A. Hayes, Jr., CPA, Director
Division of State Audit

AAH/sdr

FINDINGS AND RECOMMENDATIONS

DATA PROCESSING SECURITY WAS NOT ADEQUATE

1. FINDING:

The University of Tennessee used the Resource Access Control Facility (RACF) security application for its IBM mainframe computer system. The audit revealed some problem areas.

As noted in the prior audit, computer users with high-level system access were not required by the security system to change their passwords on a regular basis. Management concurred with the finding and stated, "We contacted each person who still has special authority and asked that they change their passwords every thirty days." However, this measure has not proven to be effective. Four users with high-level system access had not changed their passwords every 30 days. The first user had not changed the password in 327 days, the second in 173 days, the third in 48 days, and the fourth in 34 days. Good security practices require that users with high-level system access change their passwords every 30 days.

Numerous generic dataset profiles appear to allow excessive access because either the Universal Access Authority (UACC) has settings of "UPDATE" or "ALTER," or because the dataset "WARNING" option in the generic dataset profile (GDP) was set to "YES." A generic profile protects several datasets that have similar naming structures and security requirements. Universal Access Authority specifies the authority a user has to a dataset. "UPDATE" allows users to read from, copy from, or write to a dataset. "ALTER" allows users to read, update, delete, rename, or move a dataset. Setting the "WARNING" to "NO" prevents unauthorized users from accessing the protected files. Setting the "WARNING" to "YES" generates a notification to the user and the security administrator that the user is improperly accessing a protected file. However, it does not block the user from gaining such improper access. Hence a "WARNING" setting of "YES" is equivalent to no protection.

For 26 of the 61 generic profiles reviewed, either the profile contained an excessive number of "UPDATE" or "ALTER" settings or the "WARNING" option was set to "YES." Inadvertent or intentional unauthorized access to these datasets would not be prevented. Good management practices include careful consideration of the privileges resulting from settings within the GDP and the conservative use of the "WARNING" setting.

These conditions significantly increased the opportunity for misuse of computer resources for the period under review.

RECOMMENDATION:

Management should ensure that the system requires users with high-level system access to change their passwords every 30 days. In addition, management should review the protection set up for each generic dataset profile and make relevant changes to ensure that adequate controls over access are maintained.

MANAGEMENT'S COMMENT:

The University concurs with the finding. There have been two attempts to correct this problem by asking people to change their passwords and by requiring a password change if they used specific project codes. Neither was a complete success. The University will continue to require password changes from individuals with high access authority and investigate other methods of automatically enforcing these changes through the RACF system.

The numerous generic dateset profiles that have Universal Access Authority settings of UPDATE or ALTER exist because it has been deemed that the convenience of access outweighed the need for restricted access on these datasets. These datasets are backed-up twice-weekly and recoverable if problems ever occur. We have been collecting access information to develop user need profiles and will continue to monitor the situation. To the extent deemed necessary based upon this review and balanced with access convenience, relevant changes will be made to ensure adequate control.

PROGRAM CHANGE PROCEDURES WERE NOT ADEQUATE

2. FINDING:

The University of Tennessee was not requiring adequate documentation for program changes within their computerized systems. No written documentation of the policies and procedures for the program change process are available. In addition, of the 30 programs selected for review, 15 (50%) did not have required change request forms to document the various approvals and provide pertinent information necessary to adequately control the program change process. Good management practices include an established written policy for the program change process and management review to ensure these policies are implemented.

RECOMMENDATION:

Management should develop written policies and procedures for the program change process to include, at a minimum, management approval of the request, assignment of the request to a programmer, documentation of testing, documentation of review, user approval of the change, and authorization to move the changed program from test to production. Furthermore, management should ensure that these policies and procedures are implemented.

MANAGEMENT'S COMMENT:

The University concurs with the finding. This situation has evolved over the last few years as our organization has changed by combining departments. There is documentation available, but it did not reflect the current procedures as accurately as it should and it was not readily available. However, we started addressing this issue late this past summer and already have a "short-term" solution in place to address the "long-term" solution with both the state auditors and UT's internal auditors and we have heard of no problems with our plans. In addition, we now have written procedures to address the "change request" aspect of this process.

FAILURE TO PROMPTLY RETURN FINANCIAL AID REFUNDS

3. FINDING:

As noted in the last two audits, the University of Tennessee at Knoxville bursar's office did not return the federal financial aid portion of refunds to the appropriate programs or lending institutions in a timely manner. The *Code of Federal Regulations*, Section 34, Part 668.22 (g)(2)(iv), states:

> The amount of the Title IV, HEA [Higher Education Act of 1965] program portion of the refund allocated to the Title IV, HEA programs other than the FWS, Federal Stafford Loan, Federal PLUS, and Federal SLS programs must be returned to the appropriate program account or accounts by the institution within 30 days of the date that the student officially withdraws, is expelled, takes an approved leave of absence, or the institution determines that a student has unofficially withdrawn.

For Federal Family Education Loans (Stafford, SLS, or PLUS), the *Code of Federal Regulations*, Section 34, Part 682.607 (c)(1), states, "A school shall pay a refund that is due . . . within 60 days after the student's withdrawal." Five of five Pell refunds tested were not deposited into the appropriate accounts within 30 days, and 11 of 11 Federal Family Education Loan refunds tested were not returned to the lender within 60 days.

The refunds were not calculated and returned on a timely basis because university personnel were in the process of revising their refund and repayment policies to comply with Title IV regulations.

RECOMMENDATION:

The bursar's office should return the federal financial aid portion of refunds to the appropriate programs or lending institutions within the time frame specified by federal regulations.

MANAGEMENT'S COMMENT:

The University concurs with the finding. The Office of the Bursar has undertaken several projects to ensure compliance with Title IV regulations and to improve operations specified in the 1996 State Audit Report.

The Financial Aid Office and the Office of the Bursar have worked together to revise and improve UTK refund and repayment processes and calculations. The Financial Aid Office has shared several forms (Withdrawal Records, Refund Calculation Worksheet, Pro Rata Refund Calculation Worksheet and Repayment Calculation Worksheet) with the Bursar's Office. The Bursar's Office is currently using forms which were designed by the United States Department of Education. The Financial Aid Office has also provided refund/repayment calculation software which two individuals in the Bursar's Office are currently using to calculate refunds and repayments as recommended by the state auditors. Individuals from both offices have attended federal refund/repayment workshops and have met on several occasions to discuss the new process during the past year.

The University has implemented a team approach to ensure timeliness of the entire refund/repayment processes. The team effort involves Computing and Administrative Systems (CAS), Financial Aid, the Bursar's Office and the Registrar's Office.

Compliance Report Based on an Audit of the Financial Statements Performed in Accordance With *Government Auditing Standards*

September 20, 1996

The Honorable W. R. Snodgrass
Comptroller of the Treasury
State Capitol
Nashville, Tennessee 37243

Dear Mr. Snodgrass:

We have audited the financial statements of the University of Tennessee, a component unit of the State of Tennessee, as of and for the year ended June 30, 1996, and have issued our report thereon dated September 20, 1996. Our report was qualified because the university excluded the liability for accrued compensated absences from the balance sheet.

We conducted our audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

Compliance with laws, regulations, contracts, and grants applicable to the university is the responsibility of the university's management. As part of obtaining reasonable assurance about whether the financial statements are free of material misstatement, we performed tests of the university's compliance with certain provisions of laws, regulations, contracts, and grants. However, the objective of our audit of the financial statements was not to provide an opinion on overall compliance with such provisions. Accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of noncompliance that are required to be reported herein under generally accepted government auditing standards.

We did, however, note certain immaterial instances of noncompliance that we have included in the Findings and Recommendations section of this report. We also noted certain other less significant instances of noncompliance that we have reported to the university's management in a separate letter.

This report is intended for the information of the General Assembly of the State of Tennessee, the board of trustees, and management. However, this report is a matter of public record, and its distribution is not limited.

Sincerely,

Arthur A. Hayes, Jr., CPA, Director
Division of State Audit

AAH/sdr

Independent Auditor's Report

September 20, 1996

The Honorable W. R. Snodgrass
Comptroller of the Treasury
State Capitol
Nashville, Tennessee 37243

Dear Mr. Snodgrass:

We have audited the accompanying balance sheets of the University of Tennessee, which is a component unit of the State of Tennessee, as of June 30, 1996, and June 30, 1995, and the related statements of changes in fund balances and current funds revenues, expenditures, and other changes for the years then ended. These financial statements are the responsibility of the university's management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As described in Note 2 to the financial statements, the university has excluded the liability for accrued compensated absences from the accompanying balance sheets. In our opinion, accrued compensated absences should be included to conform with generally accepted accounting principles. The recognition of this liability would have increased the liabilities of the unrestricted current fund by $49,734,929.94 at June 30, 1996, and $48,109,437.06 at June 30, 1995, and increased the unrestricted current fund expenditures by $1,625,492.88 for the year ended June 30, 1996, and $3,100,377.47 for the year ended June 30, 1995.

In our opinion, except for the effects of not including the liability for accrued compensated absences in the accompanying balance sheets, as discussed in the preceding paragraph, the financial statements referred to above present fairly, in all material respects, the financial position of the University of Tennessee as of June 30, 1996, and June 30, 1995, and the changes in fund balances and the current funds revenues, expenditures, and other changes for the years then ended in conformity with generally accepted accounting principles.

In accordance with generally accepted government auditing standards, we have also issued reports dated September 20, 1996, on our consideration of the university's internal control structure and on its compliance with laws and regulations.

Sincerely,

Arthur A. Hayes, Jr., CPA, Director
Division of State Audit

AAH/sdr

Exhibit A

THE UNIVERSITY OF TENNESSEE
BALANCE SHEETS
JUNE 30, 1996, AND JUNE 30, 1995

ASSETS	June 30, 1996	June 30, 1995
Current funds:		
Unrestricted:		
General:		
Cash and cash equivalents (Note 3)	$ 93,105,849.15	$ 101,651,695.31
Accrued interest receivable	2,073,883.05	2,188,422.88
Accounts receivable (net of allowance of $2,618,817.24 at June 30, 1996, and $2,856,895.00 at June 30, 1995)	9,877,548.28	12,408,741.16
Inventories (Note 1)	5,192,583.93	4,614,146.83
Prepaid expenses and deferred charges	2,782,215.50	2,361,645.39
Due from life income funds	54,260.14	52,414.46
Total general	113,086,340.05	123,277,066.03
Auxiliary enterprises:		
Cash and cash equivalents (Note 3)	17,393,511.98	18,872,040.06
Accounts receivable (net of allowance of $1,332,295.19 at June 30, 1996, and $2,503,591.98 at June 30, 1995)	3,392,518.39	2,814,110.95
Inventories (Note 1)	5,562,350.42	4,971,643.48
Deferred charges	431,222.76	328,818.44
Total auxiliary enterprises	26,779,603.55	26,986,612.93
Hospitals:		
Cash and cash equivalents (Note 3)	28,491,074.13	24,113,191.00
Accounts receivable (net of allowance of $53,305,302.38 at June 30, 1996, and $52,015,099.91 at June 30, 1995)	68,423,874.70	68,372,908.10
Inventories (Note 1)	2,096,558.71	2,320,796.40
Deferred charges	503,087.00	217,835.67
Total hospitals	99,514,594.54	95,024,731.17
Total unrestricted	239,380,538.14	245,288,410.13
Restricted:		
Cash and cash equivalents (Note 3)	23,126,799.20	17,262,769.98
Accounts receivable - educational and general	47,579,287.17	44,896,119.33
Accounts receivable - hospitals	759,401.02	1,382,897.88
Bonds (Note 3)	12,929.54	14,051.06
Stocks (Note 3)	19,750.00	19,750.00
Other assets (Note 3)	116,097.48	133,216.63
Real estate gifts (Note 3)	385,000.00	1,265,000.00
Total restricted	71,999,264.41	64,973,804.88
Total current funds	$ 311,379,802.55	$ 310,262,215.01

LIABILITIES AND FUND BALANCES	June 30, 1996	June 30, 1995
Current funds:		
Unrestricted:		
General:		
Liabilities:		
Salaries, wages, and benefits payable	$ 12,898,127.95	$ 9,117,294.27
Accounts payable (Note 1)	33,567,402.21	43,888,981.49
Payroll taxes payable	11,336,786.02	13,406,485.58
Deposits and advance payments	1,625,048.10	1,393,622.04
Deferred revenue	9,041,065.76	8,144,711.90
Total liabilities	68,468,430.04	75,951,095.28
Fund balances:		
Nondiscretionary allocations:		
Allocation for working capital (Note 1)	13,925,127.45	15,700,833.28
Allocation for encumbrances (Note 11)	3,896,702.25	4,737,382.88
Discretionary allocations:		
Allocation for unemployment compensation	621,831.43	979,194.15
Allocation for revolving accounts	8,060,903.33	7,790,519.45
Allocation for unexpended gifts	1,796,359.07	1,606,787.63
Allocation for reappropriations	3,983,689.57	4,218,142.57
Unallocated	12,333,296.91	12,293,110.79
Total fund balances	44,617,910.01	47,325,970.75
Total general	113,086,340.05	123,277,066.03
Auxiliary enterprises:		
Liabilities:		
Salaries, wages, and benefits payable	557,934.18	31,067.03
Accounts payable	1,863,772.32	2,235,624.85
Deposits and advance payments	1,165,123.38	1,322,571.76
Deferred revenue	10,749,022.18	11,960,741.40
Total liabilities	14,335,852.06	15,550,005.04
Fund balances:		
Nondiscretionary allocations:		
Allocation for working capital (Note 1)	8,943,050.34	7,777,510.17
Allocation for encumbrances (Note 11)	597,945.30	430,647.10
Unallocated	2,902,755.85	3,228,450.62
Total fund balances	12,443,751.49	11,436,607.89
Total auxiliary enterprises	26,779,603.55	26,986,612.93
Hospitals:		
Liabilities:		
Accounts payable	14,658,388.14	11,619,042.29
Salaries, wages, and benefits payable	5,534,345.01	1,554,683.11
Total liabilities	20,192,733.15	13,173,725.40
Fund balances:		
Nondiscretionary allocations:		
Allocated for working capital (Note 1):		
Memorial Hospital - Knoxville	55,803,521.42	59,518,631.52
William F. Bowld Hospital - Memphis	14,714,893.24	11,173,162.43
Allocated for encumbrances (Note 11):		
Memorial Hospital - Knoxville	3,800,740.83	3,541,635.29
William F. Bowld Hospital - Memphis	433,359.10	590,614.35
Discretionary allocations:		
Allocated for revolving accounts	1,104,069.32	871,536.75
Unallocated		
Memorial Hospital - Knoxville	9,905,759.76	9,995,229.07
William F. Bowld Hospital - Memphis	(6,440,482.28)	(3,839,803.64)
Total fund balances	79,321,861.39	81,851,005.77
Total hospitals	99,514,594.54	95,024,731.17
Total unrestricted	239,380,538.14	245,288,410.13
Restricted:		
Liabilities:		
Salaries, wages, and benefits payable	871,585.74	289,076.01
Accounts payable	2,458,405.81	2,087,869.73
Deposits and advance payments	-	80,000.00
Total liabilities	3,329,991.55	2,456,945.74
Fund balances:		
Educational and general	65,849,568.52	59,608,826.45
Auxiliary enterprises	313,365.48	291,496.30
Hospitals	2,506,338.86	2,616,536.39
Total fund balances	68,669,272.86	62,516,859.14
Total restricted	71,999,264.41	64,973,804.88
Total current funds	$ 311,379,802.55	$ 310,262,215.01

Exhibit A (Cont.)

THE UNIVERSITY OF TENNESSEE
BALANCE SHEETS
JUNE 30, 1996, AND JUNE 30, 1995

ASSETS	June 30, 1996	June 30, 1995
Loan funds:		
Cash and cash equivalents (Note 3)	$ 5,077,745.02	$ 4,173,503.36
Accrued interest receivable	659,055.88	610,007.82
Notes receivable (net of allowance of $1,810,466.25 at June 30, 1996, and $1,805,304.75 at June 30, 1995)	29,507,061.29	29,100,010.50
Total loan funds	$ 35,243,862.19	$ 33,883,521.68
Endowment and similar funds (Note 4):		
Cash and cash equivalents (Note 3)	$ 17,007,084.83	$ 12,748,967.54
Accounts receivable	382,320.77	76,107.43
Notes receivable (Note 3)	1,733,354.95	1,704,286.94
Bonds (Note 3)	70,828,583.24	62,788,550.11
Stocks (Note 3)	80,607,406.48	74,660,625.15
Venture capital (Note 3)	7,566,026.36	5,793,990.36
Assets with the University of Chattanooga Foundation, Inc. (Notes 3 and 10)	1,601,257.00	1,348,304.00
Assets held by others (Note 3)	205,994.05	202,627.00
Real estate gifts (Note 3)	3,422,247.44	3,160,356.28
Real estate equity (Note 3)	5,962,950.00	6,003,700.00
Other assets (Note 3)	26,891.00	26,892.00
Total endowment and similar funds	$ 189,344,116.12	$ 168,514,406.81
Life income funds (Note 4):		
Cash and cash equivalents (Note 3)	$ 832,487.63	$ 392,742.72
Accounts receivable	129,427.28	8,969.97
Notes receivable (Note 3)	1,313,805.45	1,551,736.76
Bonds (Note 3)	23,088,825.82	19,718,750.66
Stocks (Note 3)	3,393,143.87	2,552,917.01
Real estate gifts (Note 3)	1,836,640.00	1,210,000.00
Total life income funds	$ 30,594,330.05	$ 25,435,117.12
Plant funds:		
Unexpended plant:		
Cash and cash equivalents (Note 3)	$ 4,799,187.23	$ -
Notes receivable (Note 3)	4,973.81	268,710.97
Real estate gifts (Note 3)	82,700.00	99,530.00
State capital outlay and maintenance receivable	406,719.15	3,416,350.19
Tennessee State School Bond Authority debt proceeds receivable	7,094,202.64	6,847,632.42
Stocks (Note 3)	886.15	1,142.37
Total unexpended plant	12,388,668.98	10,633,365.95
Retirement of indebtedness and renewals and replacements:		
Cash and cash equivalents (Note 3)	89,083,999.68	77,774,249.14
Due from unexpended plant	-	11,878,048.53
Unexpended construction earnings receivable	340,995.96	240,873.52
Assets with trustees (Note 3):		
Tennessee State School Bond Authority	22,831,998.90	22,920,053.35
Department of Education student housing reserve	175,798.18	250,247.42
Total retirement of indebtedness and renewals and replacements	112,432,792.72	113,063,471.96
Investment in plant (Note 1):		
Land	32,802,171.21	30,440,266.21
Buildings	953,030,875.63	899,966,618.57
Improvements other than buildings	69,798,317.02	63,662,404.56
Equipment	407,970,287.50	378,089,194.78
Library holdings	63,385,020.00	61,861,200.00
Livestock	1,690,348.00	1,858,940.00
Total investment in plant	1,528,677,019.36	1,435,878,624.12
Total plant funds	$ 1,653,498,481.06	$ 1,559,575,462.03
Agency funds:		
Cash and cash equivalents (Note 3)	$ 3,780,495.46	$ 3,086,671.07
Accounts receivable	368,895.87	414,311.98
Bonds (Note 3)	198,750.00	198,750.00
Stocks (Note 3)	3,269,176.38	3,505,446.00
Total agency funds	$ 7,617,317.71	$ 7,205,179.05

LIABILITIES AND FUND BALANCES	June 30, 1996	June 30, 1995
Loan funds:		
Fund balances:		
Privately sponsored loan funds - restricted	$ 4,232,906.20	$ 3,963,804.28
University funds - restricted	2,186,888.77	2,065,641.96
Federal participation loan funds - restricted	28,824,067.22	27,854,075.44
Total loan funds	$ 35,243,862.19	$ 33,883,521.68
Endowment and similar funds:		
Accounts payable	$ 403,418.92	$ 270,624.38
Fund balances:		
Undistributed gains and losses on investment transactions	39,714,120.76	32,365,487.18
Endowment - restricted	132,529,814.15	120,987,753.20
Quasi-endowment - restricted	16,344.74	16,344.74
Quasi-endowment - unrestricted	16,680,417.55	14,874,197.31
Total fund balances	188,940,697.20	168,243,782.43
Total endowment and similar funds	$ 189,344,116.12	$ 168,514,406.81
Life income funds:		
Due to unrestricted current funds - general	$ 54,260.14	$ 52,414.46
Fund balances - restricted	30,540,069.91	25,382,702.66
Total life income funds	$ 30,594,330.05	$ 25,435,117.12
Plant funds:		
Unexpended plant:		
Liabilities:		
Accounts payable	$ 5,590,904.14	$ 5,716,396.78
Due to retirement of indebtedness	-	11,878,048.53
Total liabilities	5,590,904.14	17,594,445.31
Fund balances:		
Restricted	4,348,358.26	(8,907,002.46)
Unrestricted:		
Designated	2,393,935.56	1,912,664.62
Undesignated	55,471.02	33,258.48
Total fund balances	6,797,764.84	(6,961,079.36)
Total unexpended plant	12,388,668.98	10,633,365.95
Retirement of indebtedness and renewals and replacements:		
Fund balances:		
Restricted	23,531,389.17	23,577,820.57
Unrestricted	88,901,403.55	89,485,651.39
Total retirement of indebtedness and renewals and replacements	112,432,792.72	113,063,471.96
Investment in plant:		
Liabilities:		
Tennesssee State School Bond Authority indebtedness (Note 5)	265,663,620.79	227,572,803.85
Notes payable (Note 5)	124,920.41	142,082.22
Accrued interest payable	2,047,776.60	2,257,092.62
Lease obligations (Note 7)	2,665,042.21	3,683,505.08
Fund balances:		
Net investment in plant	1,258,175,659.35	1,202,223,140.35
Total investment in plant	1,528,677,019.36	1,435,878,624.12
Total plant funds	$ 1,653,498,481.06	$ 1,559,575,462.03
Agency funds:		
Liabilities:		
Accounts payable	$ 109,950.16	$ 25,583.62
Deposits held in custody for others	7,507,367.55	7,179,595.43
Total agency funds	$ 7,617,317.71	$ 7,205,179.05

The notes to the financial statements are an integral part of this statement.

Exhibit B

THE UNIVERSITY OF TENNESSEE
STATEMENT OF CHANGES IN FUND BALANCES
FOR THE YEAR ENDED JUNE 30, 1996

	Current Funds								Plant Funds		
	Unrestricted										
	Educational and General	Auxiliary Enterprises	Hospitals	Total	Restricted	Loan Funds	Endowment and Similar Funds	Life Income Funds	Unexpended	Retirement of Indebtedness and Renewals and Replacements	Investment In Plant
REVENUES AND OTHER ADDITIONS											
Unrestricted current funds revenues	$ 566,266,308.89	$ 108,148,427.91	$ 300,974,888.79	$ 975,389,625.59	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Restricted gifts and grants	-	-	-	-	223,088,885.00	-	10,912,851.47	5,298,004.10	-	-	-
Federal Perkins loan funds	-	-	-	-	-	464,959.54	-	-	-	-	-
Federal nursing and health professions loan funds	-	-	-	-	-	119,918.51	-	-	-	-	-
Interest on notes receivable	-	-	-	-	-	757,418.97	-	-	-	-	-
Endowment income	-	-	-	-	7,258,720.12	56,334.49	313,973.26	-	-	-	-
Investment income	-	-	-	-	129,426.05	146,171.62	-	1,750,201.00	490,493.88	4,583,900.07	-
Net gain on investments	-	-	-	-	-	-	8,175,873.86	185,916.22	-	-	-
State appropriations for capital outlay	-	-	-	-	-	-	-	-	16,719,315.31	-	-
Tennessee State School Bond Authority proceeds	-	-	-	-	-	-	-	-	50,612,695.80	-	-
Capital lease acquisitions	-	-	-	-	-	-	-	-	-	-	1,023,711.23
Gifts and other sources	-	-	-	-	-	97,808.14	-	-	659,041.56	18,651.00	7,547,478.42
Student debt service fees	-	-	-	-	-	-	-	-	-	2,740,023.84	-
Federal interest subsidy grants	-	-	-	-	-	-	-	-	-	206,078.00	-
Special state legislature appropriations	-	-	-	-	-	-	-	-	-	386,119.07	-
Expended for plant facilities (including $47,829,674.35 charged to current fund expenditures)	-	-	-	-	-	-	-	-	-	-	111,256,886.27
Retirement of indebtedness	-	-	-	-	-	-	-	-	-	-	12,451,344.87
Total revenues and other additions	566,266,308.89	108,148,427.91	300,974,888.79	975,389,625.59	230,477,031.17	1,642,611.27	19,402,698.59	7,234,121.32	68,481,546.55	7,934,771.98	132,279,420.79
EXPENDITURES AND OTHER DEDUCTIONS											
Unrestricted current fund expenditures	568,567,613.90	90,487,457.38	287,523,289.89	946,578,361.17	-	-	-	-	-	-	-
Restricted current fund expenditures	-	-	-	-	205,503,165.96	-	-	-	-	-	-
Administration and collection costs	-	-	-	-	-	164,970.56	-	-	-	-	-
Loan cancellations and write-offs	-	-	-	-	-	225,669.15	-	-	-	-	-
Payments to beneficiaries	-	-	-	-	-	-	-	1,772,812.30	-	-	-
Expended for plant facilities	-	-	-	-	-	-	-	-	63,092,519.01	334,692.91	-
Retirement of indebtedness	-	-	-	-	-	-	-	-	-	12,451,344.87	-
Interest on indebtedness	-	-	-	-	-	-	-	-	-	12,824,218.61	-
Disposal of plant facilities	-	-	-	-	-	-	-	-	-	-	340,675.00
Buildings and improvements written off and adjustments	-	-	-	-	-	-	-	-	-	-	1,150,422.14
Physical inventory adjustments	-	-	-	-	-	-	-	-	-	-	24,305,556.29
Capital lease additions	-	-	-	-	-	-	-	-	-	-	5,248.36
Bonds and notes issued	-	-	-	-	-	-	-	-	-	-	50,525,000.00
Indirect costs recovered	-	-	-	-	18,856,452.57	-	-	-	-	-	-
Other	-	-	-	-	819,417.18	22,914.02	750.00	3,900.21	5,646,078.26	-	-
Total expenditures and other deductions	568,567,613.90	90,487,457.38	287,523,289.89	946,578,361.17	225,179,035.71	413,553.73	750.00	1,776,712.51	68,738,597.27	25,610,256.39	76,326,901.79

Exhibit B (Cont.)

THE UNIVERSITY OF TENNESSEE
STATEMENT OF CHANGES IN FUND BALANCES
FOR THE YEAR ENDED JUNE 30, 1996

	Current Funds								Plant Funds		
	Unrestricted										
	Educational and General	Auxiliary Enterprises	Hospitals	Total	Restricted	Loan Funds	Endowment and Similar Funds	Life Income Funds	Unexpended	Retirement of Indebtedness and Renewals and Replacements	Investment In Plant
TRANSFERS AMONG FUNDS - ADDITIONS (DEDUCTIONS)											
Mandatory:											
Prinicipal and interest	(2,100,400.50)	(8,802,783.47)	(9,357,177.39)	(20,260,361.36)	-	-	-	-	-	20,260,361.36	-
Loan funds matching	(117,705.70)	-	-	(117,705.70)	-	117,705.70	-	-	-	-	-
Endowment and similar funds	-	-	-	-	-	-	300,041.56	(300,041.56)	-	-	-
Nonmandatory:											
Unrestricted current funds	5,081,869.87	(3,372,574.84)	(1,709,295.03)	-	-	-	-	-	-	-	-
Restricted current funds	(511,824.06)	(56,056.00)	49,529.71	(518,350.35)	854,418.26	13,577.27	(197,671.00)	-	(151,974.18)	-	-
Endowment and similar funds	(10,500.00)	-	(157,496.00)	(167,996.00)	-	-	167,996.00	-	-	-	-
Unexpended plant	(1,203,494.95)	(1,725,112.29)	(4,806,304.57)	(7,734,911.81)	-	-	-	-	14,167,869.10	(6,432,957.29)	-
Retirement of indebtedness	(1,544,700.39)	(2,697,300.33)		(4,242,000.72)	-	-	1,024,599.62	-	-	3,217,401.10	-
Total transfers	(406,755.73)	(16,653,826.93)	(15,980,743.28)	(33,041,325.94)	854,418.26	131,282.97	1,294,966.18	(300,041.56)	14,015,894.92	17,044,805.17	-
Net increase (decrease) for the year	(2,708,060.74)	1,007,143.60	(2,529,144.38)	(4,230,061.52)	6,152,413.72	1,360,340.51	20,696,914.77	5,157,367.25	13,758,844.20	(630,679.24)	55,952,519.00
Fund balance at July 1, 1995	47,325,970.75	11,436,607.89	81,851,005.77	140,613,584.41	62,516,859.14	33,883,521.68	168,243,782.43	25,382,702.66	(6,961,079.36)	113,063,471.96	1,202,223,140.35
Fund balance at June 30, 1996	$ 44,617,910.01	$ 12,443,751.49	$ 79,321,861.39	$ 136,383,522.89	$ 68,669,272.86	$ 35,243,862.19	$ 188,940,697.20	$ 30,540,069.91	$ 6,797,764.84	$ 112,432,792.72	$ 1,258,175,659.35

The notes to the financial statements are an integral part of this statement.

Exhibit C

THE UNIVERSITY OF TENNESSEE
STATEMENT OF CHANGES IN FUND BALANCES
FOR THE YEAR ENDED JUNE 30, 1995

	Current Funds								Plant Funds		
	Unrestricted										
	Educational and General	Auxiliary Enterprises	Hospitals	Total	Restricted	Loan Funds	Endowment and Similar Funds	Life Income Funds	Unexpended	Retirement of Indebtedness and Renewals and Replacements	Investment In Plant
<u>REVENUES AND OTHER ADDITIONS</u>											
Unrestricted current funds revenues	$ 557,631,330.80	$ 102,197,623.97	$ 299,598,578.68	$ 959,427,533.45	$ -	$ -	$ -	$ -	$ -	$ -	$ -
Restricted gifts and grants	-	-	-	-	222,632,827.36	-	11,791,902.17	3,296,167.98	-	-	-
Federal Perkins loan funds	-	-	-	-	-	407,550.00	-	-	-	-	-
Federal nursing and health professions loan funds	-	-	-	-	-	178,327.00	-	-	-	-	-
Interest on notes receivable	-	-	-	-	-	777,536.65	-	-	-	-	-
Endowment income	-	-	-	-	7,338,018.75	52,198.73	287,194.43	-	-	-	-
Investment income	-	-	-	-	90,034.35	111,890.54	-	1,576,809.54	528,486.29	3,304,025.38	-
Net gain on investments	-	-	-	-	-	-	4,635,821.79	161,547.97	-	-	-
State appropriations for capital outlay	-	-	-	-	-	-	-	-	17,858,250.04	-	-
Tennessee State School Bond Authority proceeds	-	-	-	-	-	-	-	-	12,233,131.23	-	-
Capital lease acquisitions	-	-	-	-	-	-	-	-	-	-	344,255.54
Gifts and other sources	-	-	-	-	-	73,276.18	-	-	1,832,365.02	-	4,881,933.43
Student debt service fees	-	-	-	-	-	-	-	-	-	2,155,445.93	-
Federal interest subsidy grants	-	-	-	-	-	-	-	-	-	206,078.00	-
Special state legislature appropriations	-	-	-	-	-	-	-	-	-	405,408.68	-
Expended for plant facilities (including $42,119,533.21 charged to current fund expenditures)	-	-	-	-	-	-	-	-	-	-	94,584,122.95
Retirement of indebtedness	-	-	-	-	-	-	-	-	-	-	12,494,836.36
Total revenues and other additions	557,631,330.80	102,197,623.97	299,598,578.68	959,427,533.45	230,060,880.46	1,600,779.10	16,714,918.39	5,034,525.49	32,452,232.58	6,070,957.99	112,305,148.28
<u>EXPENDITURES AND OTHER DEDUCTIONS</u>											
Unrestricted current fund expenditures	555,988,486.30	88,160,246.92	284,610,004.68	928,758,737.90	-	-	-	-	-	-	-
Restricted current fund expenditures	-	-	-	-	205,050,192.56	-	-	-	-	-	-
Administration and collection costs	-	-	-	-	-	14,577.40	-	-	-	-	-
Loan cancellations and write-offs	-	-	-	-	-	64,151.38	-	-	-	-	-
Payments to beneficiaries	-	-	-	-	-	-	-	1,571,924.23	-	-	-
Expended for plant facilities	-	-	-	-	-	-	-	-	52,375,117.67	89,472.07	-
Retirement of indebtedness	-	-	-	-	-	-	-	-	-	12,494,836.36	-
Interest on indebtedness	-	-	-	-	-	-	-	-	-	12,718,984.96	-
Disposal of plant facilities	-	-	-	-	-	-	-	-	-	-	153,625.00
Buildings and improvements written off and adjustments	-	-	-	-	-	-	-	-	-	-	781,010.00
Physical inventory adjustments	-	-	-	-	-	-	-	-	-	-	33,490,950.11
Capital lease additions	-	-	-	-	-	-	-	-	-	-	3,602,722.85
Bonds and notes issued	-	-	-	-	-	-	-	-	-	-	12,840,000.00
Indirect costs recovered	-	-	-	-	19,166,180.28	-	-	-	-	-	-
Other	-	-	-	-	737,546.49	237,947.83	12.00	2,024.00	6,388,284.38	-	-
Total expenditures and other deductions	555,988,486.30	88,160,246.92	284,610,004.68	928,758,737.90	224,953,919.33	316,676.61	12.00	1,573,948.23	58,763,402.05	25,303,293.39	50,868,307.96

Exhibit C

THE UNIVERSITY OF TENNESSEE
STATEMENT OF CHANGES IN FUND BALANCES
FOR THE YEAR ENDED JUNE 30, 1995

	Current Funds								Plant Funds		
	Unrestricted										
	Educational and General	Auxiliary Enterprises	Hospitals	Total	Restricted	Loan Funds	Endowment and Similar Funds	Life Income Funds	Unexpended	Retirement of Indebtedness and Renewals and Replacements	Investment In Plant
TRANSFERS AMONG FUNDS - ADDITIONS (DEDUCTIONS)											
Mandatory:											
Principal and interest	(2,013,487.34)	(9,232,444.64)	(9,735,661.74)	(20,981,593.72)	-	-	-	-	-	20,981,593.72	-
Loan funds matching	(114,489.68)	-	-	(114,489.68)	-	639,572.94	-	(525,083.26)	-	-	-
Endowment and similar funds	-	-	-	-	-	-	386,787.85	(386,787.85)	-	-	-
Restricted current funds	-	-	-	-	16,238.27	-	-	(16,238.27)	-	-	-
Nonmandatory:											
Unrestricted current funds	4,427,760.44	(2,977,560.44)	(1,450,200.00)	-	-	-	-	-	-	-	-
Restricted current funds	(537,327.85)	-	55,764.31	(481,563.54)	539,790.88	20,535.00	(766,529.27)	-	687,766.93	-	-
Endowment and similar funds	(1,242.08)	-	(119,997.00)	(121,239.08)	-	-	121,239.08	-	-	-	-
Unexpended plant	(1,105,281.06)	(783,453.53)	(4,451,753.43)	(6,340,488.02)	-	-	-	-	15,163,511.53	(8,823,023.51)	-
Retirement of indebtedness	(91,718.10)	(2,553,684.13)		(2,645,402.23)	-	-	-	-	-	2,645,402.23	-
Total transfers	564,214.33	(15,547,142.74)	(15,701,847.86)	(30,684,776.27)	556,029.15	660,107.94	(258,502.34)	(928,109.38)	15,851,278.46	14,803,972.44	-
Net increase (decrease) for the year	2,207,058.83	(1,509,765.69)	(713,273.86)	(15,980.72)	5,662,990.28	1,944,210.43	16,456,404.05	2,532,467.88	(10,459,891.01)	(4,428,362.96)	61,436,840.32
Fund balance at July 1, 1994	45,118,911.92	12,946,373.58	82,564,279.63	140,629,565.13	56,853,868.86	31,939,311.25	151,787,378.38	22,850,234.78	3,498,811.65	117,491,834.92	1,140,786,300.03
Fund balance at June 30, 1995	$ 47,325,970.75	$ 11,436,607.89	$ 81,851,005.77	$ 140,613,584.41	$ 62,516,859.14	$ 33,883,521.68	$ 168,243,782.43	$ 25,382,702.66	$ (6,961,079.36)	$ 113,063,471.96	$ 1,202,223,140.35

The notes to the financial statements are an integral part of this statement.

Exhibit D

THE UNIVERSITY OF TENNESSEE
STATEMENT OF CURRENT FUNDS REVENUES, EXPENDITURES, AND OTHER CHANGES
FOR THE YEAR ENDED JUNE 30, 1996

	Current Year		
	Unrestricted	Restricted	Total
REVENUES			
Tuition and fees	$ 120,943,753.10	$ -	$ 120,943,753.10
Federal appropriations	13,073,132.00	-	13,073,132.00
State appropriations	354,693,300.00	9,098,007.73	363,791,307.73
Local appropriations	2,086,444.16	-	2,086,444.16
Federal grants and contracts	15,538,357.99	81,339,647.57	96,878,005.56
State grants and contracts	1,459,069.77	25,714,529.49	27,173,599.26
Local grants and contracts	3,083,783.46	4,963,518.48	8,047,301.94
Private gifts, grants, and contracts	4,180,015.16	68,371,464.47	72,551,479.63
Endowment income - university and other	57,465.82	11,242,713.44	11,300,179.26
Sales and services of educational activities	33,280,889.18	-	33,280,889.18
Other sources	17,870,098.25	-	17,870,098.25
Total educational and general	566,266,308.89	200,729,881.18	766,996,190.07
Sales and services of auxiliary enterprises	108,148,427.91	11,934.83	108,160,362.74
Sales and services of hospitals	300,974,888.79	4,761,349.95	305,736,238.74
Total current revenues	975,389,625.59	205,503,165.96	1,180,892,791.55
EXPENDITURES AND TRANSFERS			
Educational and general expenditures:			
Instruction	262,870,050.51	46,146,082.85	309,016,133.36
Research	36,684,913.41	87,921,582.70	124,606,496.11
Public service	45,973,988.02	36,208,228.15	82,182,216.17
Academic support	64,854,570.40	4,459,117.60	69,313,688.00
Student services	35,944,244.74	931,912.86	36,876,157.60
Institutional support	57,842,371.20	479,081.75	58,321,452.95
Operation and maintenance of plant	47,768,186.97	34,627.01	47,802,813.98
Scholarships and fellowships	16,629,288.65	24,549,248.26	41,178,536.91
Total educational and general expenditures	568,567,613.90	200,729,881.18	769,297,495.08
Mandatory transfers for:			
Principal and interest	2,100,400.50	-	2,100,400.50
Loan funds	117,705.70	-	117,705.70
Nonmandatory transfers for:			
Retirement of indebtedness	1,544,700.39	-	1,544,700.39
Endowment and similar funds	10,500.00	-	10,500.00
Restricted current funds	511,824.06	-	511,824.06
Unexpended plant	1,203,494.95	-	1,203,494.95
Auxiliary enterprises	(3,372,574.84)	-	(3,372,574.84)
Hospitals	(1,709,295.03)	-	(1,709,295.03)
Total educational and general expenditures and transfers	568,974,369.63	200,729,881.18	769,704,250.81
Auxiliary enterprises:			
Expenditures	90,487,457.38	11,934.83	90,499,392.21
Mandatory transfer for:			
Principal and interest	8,802,783.47	-	8,802,783.47
Nonmandatory transfers for:			
Retirement of indebtedness	2,697,300.33	-	2,697,300.33
Unexpended plant	1,725,112.29	-	1,725,112.29
Restricted current funds	56,056.00	-	56,056.00
Educational and general	3,372,574.84	-	3,372,574.84
Total auxiliary enterprises expenditures and transfers	107,141,284.31	11,934.83	107,153,219.14
Hospitals:			
Expenditures	287,523,289.89	4,761,349.95	292,284,639.84
Mandatory transfer for:			
Principal and interest	9,357,177.39	-	9,357,177.39
Nonmandatory transfers for:			
Educational and general	1,709,295.03	-	1,709,295.03
Endowment and similar funds	157,496.00	-	157,496.00
Restricted current funds	(49,529.71)	-	(49,529.71)
Unexpended plant	4,806,304.57	-	4,806,304.57
Total hospitals expenditures and transfers	303,504,033.17	4,761,349.95	308,265,383.12
Total expenditures and transfers	979,619,687.11	205,503,165.96	1,185,122,853.07
Excess (deficiency) revenues over (under) expenditures and transfers:			
Educational and general	(2,708,060.74)	-	(2,708,060.74)
Auxiliary enterprises	1,007,143.60	-	1,007,143.60
Hospitals	(2,529,144.38)	-	(2,529,144.38)
OTHER TRANSFERS AND ADDITIONS (DEDUCTIONS)			
Restricted receipts in excess of expenditures	-	24,973,865.21	24,973,865.21
Indirect costs recovered	-	(18,856,452.57)	(18,856,452.57)
Restricted gifts transferred from (to) other funds	-	35,001.08	35,001.08
Net increase (decrease) in fund balances	$ (4,230,061.52)	$ 6,152,413.72	$ 1,922,352.20

The notes to the financial statements are an integral part of this statement.

THE UNIVERSITY OF TENNESSEE
STATEMENT OF CURRENT FUNDS REVENUES, EXPENDITURES, AND OTHER CHANGES
FOR THE YEAR ENDED JUNE 30, 1995

	Current Year		
	Unrestricted	Restricted	Total
REVENUES			
Tuition and fees	$ 116,939,537.49	$ -	$ 116,939,537.49
Federal appropriations	13,088,358.62	-	13,088,358.62
State appropriations	344,820,624.00	9,301,180.58	354,121,804.58
Local appropriations	2,031,653.36	-	2,031,653.36
Federal grants and contracts	15,817,495.33	86,276,783.34	102,094,278.67
State grants and contracts	1,313,148.67	23,388,398.04	24,701,546.71
Local grants and contracts	3,458,577.87	4,863,264.77	8,321,842.64
Private gifts, grants, and contracts	4,315,799.40	65,621,001.02	69,936,800.42
Endowment income - university and other	67,442.33	10,803,017.70	10,870,460.03
Sales and services of educational activities	36,627,364.57	-	36,627,364.57
Other sources	19,151,329.16	-	19,151,329.16
Total educational and general funds revenues	557,631,330.80	200,253,645.45	757,884,976.25
Sales and services of auxiliary enterprises	102,197,623.97	18,842.82	102,216,466.79
Sales and services of hospitals	299,598,578.68	4,777,704.29	304,376,282.97
Total current revenues	959,427,533.45	205,050,192.56	1,164,477,726.01
EXPENDITURES AND TRANSFERS			
Educational and general expenditures:			
Instruction	261,976,197.97	45,699,654.83	307,675,852.80
Organized research	35,285,625.34	93,515,310.33	128,800,935.67
Public service	47,680,264.40	32,647,812.98	80,328,077.38
Academic support	63,683,953.69	4,019,504.11	67,703,457.80
Student services	34,885,490.15	996,503.33	35,881,993.48
Institutional support	50,502,267.84	482,378.64	50,984,646.48
Operation and maintenance of physical plant	46,450,265.78	14,350.02	46,464,615.80
Scholarships and fellowships	15,524,421.13	22,878,131.21	38,402,552.34
Educational and general expenditures	555,988,486.30	200,253,645.45	756,242,131.75
Mandatory transfers for:			
Retirement of indebtedness	2,013,487.34	-	2,013,487.34
Loan funds	114,489.68	-	114,489.68
Nonmandatory transfers for:			
Retirement of indebtedness	91,718.10	-	91,718.10
Endowment and similar funds	1,242.08	-	1,242.08
Restricted current funds	537,327.85	-	537,327.85
Unexpended plant	1,105,281.06	-	1,105,281.06
Loan funds	-	-	-
Auxiliary enterprises	(2,977,560.44)	-	(2,977,560.44)
Hospitals	(1,450,200.00)	-	(1,450,200.00)
Total educational and general expenditures and transfers	555,424,271.97	200,253,645.45	755,677,917.42
Auxiliary enterprises:			
Expenditures	88,160,246.92	18,842.82	88,179,089.74
Mandatory transfers for:			
Retirement of indebtedness	9,232,444.64	-	9,232,444.64
Nonmandatory transfers for:			
Retirement of indebtedness	2,553,684.13	-	2,553,684.13
Unexpended plant	783,453.53	-	783,453.53
Educational and general	2,977,560.44	-	2,977,560.44
Total auxiliary enterprises expenditures and transfers	103,707,389.66	18,842.82	103,726,232.48
Hospitals:			
Expenditures	284,610,004.68	4,777,704.29	289,387,708.97
Mandatory transfers for:			
Retirement of indebtedness	9,735,661.74	-	9,735,661.74
Nonmandatory transfers for:			
Educational and general	1,450,200.00	-	1,450,200.00
Endowment and similar funds	119,997.00	-	119,997.00
Restricted current funds	(55,764.31)	-	(55,764.31)
Unexpended plant	4,451,753.43	-	4,451,753.43
Retirement of indebtedness	-	-	-
Total hospitals expenditures and transfers	300,311,852.54	4,777,704.29	305,089,556.83
Total current expenditures and transfers	959,443,514.17	205,050,192.56	1,164,493,706.73
Excess (deficiency) current revenues over (under) current expenditures and transfers:			
Educational and general	2,207,058.83	-	2,207,058.83
Auxiliary enterprises	(1,509,765.69)	-	(1,509,765.69)
Hospitals	(713,273.86)	-	(713,273.86)
OTHER TRANSFERS AND ADDITIONS (DEDUCTIONS)			
Restricted receipts in excess of expenditures	-	25,010,687.90	25,010,687.90
Indirect costs recovered	-	(19,166,180.28)	(19,166,180.28)
Restricted gifts transferred from (to) other funds	-	(181,517.34)	(181,517.34)
Net increase (decrease) in fund balances	$ (15,980.72)	$ 5,662,990.28	$ 5,647,009.56

The notes to the financial statements are an integral part of this statement.

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The university is a component unit of the State of Tennessee and is discretely presented in the *Tennessee Comprehensive Annual Financial Report*. Although the university is a separate legal entity, the state is financially accountable for the university because the state appoints a majority of its governing body and is obligated to provide financial support.

The University of Tennessee System is composed of the University of Tennessee, Knoxville; the University of Tennessee at Chattanooga; the University of Tennessee at Martin; the University of Tennessee - Center for the Health Sciences, composed of the Memphis campus, the Memorial Research Center at Knoxville, Clinical Education Centers at Chattanooga and Knoxville, Family Practice Centers at Jackson, Knoxville, and Memphis, and hospitals in Knoxville and Memphis; the University of Tennessee Space Institute at Tullahoma; the University of Tennessee Institute of Agriculture, composed of the College of Agriculture at Knoxville, the Agricultural Experiment Stations, the Agricultural Extension Service, and the College of Veterinary Medicine at Knoxville; the Institute for Public Service, which includes the County Technical Assistance Service and the Municipal Technical Advisory Service; and the University-Wide Administration. The university is governed by a board of 19 members, all appointed by the Governor, including one student member who also serves as Chairman. The President is the Chief Executive Officer of the university system.

Basis of Presentation

The financial statements for the University of Tennessee are prepared in accordance with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board. The university uses the AICPA College Guide model for accounting and financial reporting.

Basis of Accounting

The financial statements of the University of Tennessee have been prepared on the accrual basis except that depreciation on plant assets is not recorded and revenues and expenditures of an academic term encompassing more than one fiscal year are reported solely in the fiscal year in which the term is predominately conducted. All unrestricted resources are reported as revenue in the year they are received or earned. All restricted resources are recorded as additions to the fund balances of the appropriate fund groups. Restricted current resources are then recorded as revenues during the period in which they are expended. The statement of current funds revenues, expenditures, and other changes is a statement of financial activities of current funds related to the current reporting period. It does not purport to represent results of operations or the net income or loss for the period as would a statement of income or a statement of revenues and expenses.

To the extent that current funds are used to finance plant assets, the amounts are accounted for as (1) expenditures, for normal replacement of movable equipment and library holdings; (2) mandatory transfers, for required debt amortization and interest and equipment renewal and replacement; and (3) nonmandatory transfers for all other cases.

Fund Accounting

To ensure observance of limitations and restrictions placed on the use of resources available, the university maintains accounts in accordance with the principles of fund accounting. With this procedure, resources for various purposes are classified for accounting and reporting purposes into funds for specified activities or objectives. Separate accounts are maintained for each fund; however, in the accompanying financial statements, funds with similar characteristics have been combined into fund groups. Accordingly, all financial transactions have been recorded and reported by fund group. Within each fund group, fund balances restricted by outside sources are so indicated and are distinguished from unrestricted funds which are allocated to specific purposes by the governing board. Externally restricted funds may be used only in accordance with the purposes established by the source of such funds and contrast with unrestricted funds over which the governing board retains full control to use in achieving any of its institutional purposes. The allocations of fund balances for unemployment compensation, revolving accounts, unexpended gifts, and reappropriation were made in accordance with university policies. All gains and losses arising from the sale, collection, or other disposition of investments and other non-cash assets are accounted for in the fund that owned such assets. Ordinary income derived from investments, receivables, and the like is accounted for in the fund owning such assets, except for income derived from investments of endowment and similar funds. This income is accounted for in the fund to which it is restricted or, if unrestricted, as revenues in unrestricted current funds.

All other unrestricted revenue is accounted for in the unrestricted current funds. Restricted gifts, grants, appropriations, endowment income, and other restricted resources are accounted for in the appropriate restricted funds. Restricted current funds are reported as revenues and expenditures when expended for current operating purposes.

Current Funds - Unrestricted current funds consist of those funds over which the university retains full control for use in achieving any of its authorized institutional purposes. Auxiliary enterprises activities are included in unrestricted current funds and include student housing, bookstores, food services, parking services, and certain other activities. Hospital activities are also included in unrestricted current funds. Restricted current funds are externally restricted and may be used only in accordance with the purposes established by their source.

Loan Funds - Loan funds consist of resources made available for student loans.

Endowment and Similar Funds - Endowment funds are subject to the restrictions of gift instruments requiring in perpetuity that the principal be invested and only the income be used. Although quasi-endowment funds have been established by the governing board for the same purpose as endowment funds, a portion of quasi-endowment funds may be expended. Since these funds are internally designated, the governing board retains the right to alter or amend such designation.

Life Income Funds - Life income funds are funds held in trust by the university under agreement with donors whereby designated beneficiaries receive specified interests in annual income of the trust. Upon death of the beneficiaries or other termination of the trust, such trust assets become available to the university for use as set forth in each agreement.

Plant Funds - The plant funds consist of (1) unexpended plant funds which are to be used for the construction or acquisition of physical properties for institutional purposes; (2) retirement of indebtedness and renewal and replacement funds, which are funds set aside for debt service charges and for the retirement of indebtedness on institutional properties, and major maintenance items on institutional properties, respectively; and (3) investment in plant funds expended for, and thus invested in, institutional properties.

Agency Funds - The university acts solely as an agent in the handling of these funds; consequently, transactions of these funds do not affect the university's operating statements.

Inventories

Inventories are valued at cost, which is lower than market, based on the retail method, the average cost method, or FIFO. Cost methods are applied on a basis consistent with prior years.

Investments

Investments are recorded at cost, if purchased, or fair market value at the date of receipt, if received as a gift.

Investment in Plant

Physical plant, equipment, and land are stated at cost at date of purchase or at fair value at date of donation. Depreciation on physical plant and equipment is not recorded. Purchases of library books are recorded as current fund expenditures and capitalized at standardized costs in the plant funds. Livestock is valued at estimated market value.

Accounts Payable

Included in unrestricted current funds–general accounts payable are checks payable in the amount of $12,077,919.70 and $20,774,890.34 as of June 30, 1996, and June 30, 1995, respectively. These amounts represent the sum of checks written in excess of the university's checking account balance because of the use of a controlled disbursement account. In this way, the university maximizes interest income by transferring from an investment account only funds necessary to cover the checks that clear the bank daily.

Allocation for Working Capital

The unrestricted fund balance is allocated for the amount of working capital. Working capital is defined as the total of all petty cash, accounts receivable, inventories, and prepaid expenses in the unrestricted current fund at the balance sheet date except for student receivables credited to deferred revenue, accrued interest, accrued benefits, and amounts due on federal letters of credit.

Income Taxes

The university, as a public corporation and an instrumentality of the State of Tennessee, is exempt from federal income taxes under Section 115 of the *Internal Revenue Code*. Contributions to the university are deductible by donors as provided under Section 170 of the *Internal Revenue Code*.

NOTE 2. COMPENSATED ABSENCES

The university's employees accrue annual leave at varying rates, depending on length of service or classification. Some employees also earn compensatory time. Generally accepted accounting principles require that certain accrued vacation benefits, the effects of which are material to the financial statements, be recorded as earned. The university's policy is to record such benefits as paid. This policy is not considered a material departure from generally accepted accounting principles in that the effect of accruing the $49,734,929.94 of such benefits, of which approximately $11,119,330.01 would be reflected as a reduction of beginning unrestricted current fund balance, and the remainder would be funded from other sources, is not considered material. The amount of accrued annual leave benefits as of June 30, 1995, was $48,109,437.06, of which approximately $11,059,353.28 would have been reflected as a reduction of beginning unrestricted current fund balance, and the remainder funded from other sources.

NOTE 3. DEPOSITS AND INVESTMENTS

Investment Policy

The University of Tennessee maintains in unrestricted current funds a cash management investment pool that is available for use by all fund groups. State statutes and university investment policies authorize the university's cash management pool to invest in collateralized Tennessee bank or savings and loan association certificates of deposit, U. S. treasury obligations, U. S. government agency obligations, repurchase agreements of those securities, highest quality commercial paper, prime bankers' acceptances, and money market mutual funds meeting certain criteria.

In accordance with state statutes, commercial banks and savings and loan associations have pledged securities with third parties as collateral to secure university time and demand deposits. Market values of these securities are regularly monitored to ascertain that 105% of university deposits, less the amounts protected by the Federal Deposit Insurance Corporation, are secured.

Two categories of university funds are subject to long-term investment: the endowment and similar funds and the life income funds. The investment of these funds is governed by the gift instrument and the investment policies established by the Board of Trustees. For a more complete description of these investments, please refer to Note 4, "Endowment and Similar Funds and Life Income Funds."

Cash and Cash Equivalents

In addition to petty cash and demand deposits, this classification includes instruments which are readily convertible to known amounts of cash. At June 30, 1996, cash and cash equivalents consisted of $8,337,312.48 in bank accounts, $1,296,722.00 of petty cash on hand, $2,340,000.00 of certificates of deposit, and $265,651,918.25 in the university's cash management investment pool. At June 30, 1995, cash and cash equivalents consisted of $8,483,569.53 in bank accounts, $1,298,592.34 of petty cash on hand, $2,710,000.00 of certificates of deposit, and $243,785,787.36 in the university's cash management investment pool. Additionally, the university maintains custodial accounts at First Tennessee Bank for funds contractually managed by independent investment counsel. In accordance with the custody agreement, First Tennessee Bank placed cash equivalents of $5,072,281.58 at June 30, 1996, and $3,797,880.95 at June 30, 1995, in the bank's money market mutual fund.

Deposits

Deposits with financial institutions are required to be categorized to indicate the level of custodial risk assumed by the university. Category 1 consists of deposits that are insured or collateralized with securities held by the university or by its agent in the university's name. Category 2 consists of deposits collateralized with securities held by the pledging financial institution's trust department or agent in the university's name. Category 3 deposits are uncollateralized. This category includes any bank balance that is collateralized with securities held by the pledging financial institution or by its trust department or agent but not in the university's name.

At June 30, 1996, the carrying amount of the university's deposits was $10,677,312.48, and the bank balance including accrued interest was $7,281,435.45. The entire bank balance was category 1.

At June 30, 1995, the carrying amount of the university's deposits was $11,193,569.53, and the bank balance including accrued interest was $10,354,086.77. At June 30, 1995, $10,343,644.59 is reported as category 1, and $10,442.18 is reported as category 3.

The laws of the State of Tennessee require that collateral be pledged to secure all uninsured deposits.

Cash Management Investment Pool

The cash management investment pool consists of marketable securities and government repurchase agreements as previously described. The carrying amount and market value of the cash management pool at June 30, 1996, were $265,651,918.25 and $262,350,507.97, respectively. The carrying amount and market value of the cash management pool at June 30, 1995, were $243,785,787.36 and $245,056,136.25, respectively. The securities in the pool are categorized on the following page and listed as cash equivalents to indicate the level of risk assumed by the university. The university's standard "Master Repurchase Agreements" require that the securities underlying repurchase agreements have fair value equal to or exceeding 100% of the cost of the repurchase agreement and be delivered to its agent's trust account at the Federal Reserve Bank–Memphis. The fair value of securities underlying repurchase agreements was $43,917,229.45 at June 30, 1996, and $32,476,584.25 at June 30, 1995.

Investments

Investments shown on the balance sheet are classified by type of investment (bonds, stocks, real estate, etc.).

The university's investments are categorized below to indicate the level of custodial risk assumed by the university at year end. Category 1 consists of insured or registered investments or investments for which the securities are held by the university or its agent in the university's name. Category 2 consists of uninsured or unregistered investments for which the securities are held by the counterparty's trust department or agent in the university's name. Category 3 consists of uninsured and unregistered investments for which the securities are held by the counterparty or by its trust department or agent but not in the university's name.

June 30, 1996

	Category 1	Category 2	Category 3	Carrying Amount	Market Value
Cash equivalents					
Government securities	$ 133,700,088.81	$ -	$ -	$ 133,700,088.81	$ 130,029,297.97
Repurchase agreements	43,000,000.00	-	-	43,000,000.00	43,000,000.00
Commercial paper	88,951,829.44	-	-	88,951,829.44	89,321,210.00
	$ 265,651,918.25	$ -	$ -	$ 265,651,918.25	$ 262,350,507.97
Investments					
Domestic securities					
Government securities	$ 45,617,236.35	$ -	$ -	$ 45,617,236.35	$ 47,533,895.98
Corporate bonds	42,023,579.71	12,929.54	-	42,036,509.25	40,298,914.57
Corporate stocks	73,583,954.97	-	-	73,583,954.97	116,079,367.92
Mortgages and notes	3,041,396.10	-	10,738.11	3,052,134.21	3,078,380.38
Other investments	29,059.00	-	-	29,059.00	29,059.00
International securities					
Government bonds	375,000.00	-	-	375,000.00	351,400.00
Corporate bonds	1,100,343.00	-	-	1,100,343.00	1,098,356.90
Corporate stocks	2,471,005.09	-	-	2,471,005.09	2,361,145.40
	$ 168,241,574.22	$ 12,929.54	$ 10,738.11	$ 168,265,241.87	$ 210,830,520.15
	$ 433,893,492.47	$ 12,929.54	$ 10,738.11		

University cash equivalents and investments not susceptible to categorization:

	Carrying Amount	Market Value
Cash equivalents - assets with First Tennessee Bank as custodian	$ 5,072,281.58	$ 5,072,281.58
Limited partnership - venture capital funds	7,566,026.36	8,251,234.02
Mutual funds	3,235,402.82	4,137,129.14
Real estate equity funds	5,962,950.00	5,402,943.08
Real estate gifts	5,726,587.44	5,761,134.93
International equity fund	8,000,000.00	11,916,180.81
Assets with the University of Chattanooga Foundation	1,601,257.00	1,601,257.00
Assets with First American Bank	113,929.48	124,901.66
Assets with American National Bank	205,994.05	303,385.89
Domestic bond fund	5,000,000.00	5,052,918.50
Total investments and cash equivalents	$ 476,401,588.85	$ 520,804,394.73
Less: Cash equivalents	270,724,199.83	
Total investments on the balance sheet	$ 205,677,389.02	

June 30, 1995

	Category 1	Category 2	Carrying Amount	Market Value
Cash equivalents				
Government securities	$ 138,538,261.25	$ -	$ 138,538,261.25	$ 139,341,446.25
Repurchase agreements	32,000,000.00	210,000.00	32,210,000.00	32,210,000.00
Commercial paper	73,037,526.11	-	73,037,526.11	73,504,690.00
	$ 243,575,787.36	$ 210,000.00	$ 243,785,787.36	$ 245,056,136.25
Investments				
Domestic securities				
Government securities	$ 31,935,889.54	$ -	$ 31,935,889.54	$ 33,144,898.42
Corporate bonds	44,169,268.23	13,131.06	44,182,399.29	44,987,693.20
Corporate stocks	69,132,687.05	40,716.25	69,173,403.30	96,501,532.85
Mortgages and notes	3,549,099.25	-	3,549,099.25	3,665,748.65
Other investments	29,060.00	-	29,060.00	29,060.00
International securities				
Government bonds	501,470.00	-	501,470.00	477,840.00
Corporate bonds	1,100,343.00	-	1,100,343.00	1,094,930.75
Corporate stocks	1,783,409.22	-	1,783,409.22	1,853,425.00
	$ 152,201,226.29	$ 53,847.31	$ 152,255,073.60	$ 181,755,128.87
	$ 395,777,013.65	$ 263,847.31		

University cash equivalents and investments not susceptible to categorization:

	Carrying Amount	Market Value
Cash equivalents - assets with First Tennessee Bank as custodian	$ 3,797,880.95	$ 3 ,797,880.95
Limited partnership - venture capital funds	5,793,990.36	5,097,402.94
Mutual funds	2,283,068.01	2,624,857.38
Real estate equity funds	6,003,700.00	5,638,962.79
Real estate gifts	5,734,886.28	5,446,193.75
International equity fund	7,500,000.00	9,391,133.59
Assets with the University of Chattanooga Foundation	1,348,304.00	1,348,304.00
Assets with First American Bank	106,684.05	108,981.50
Assets with American National Bank	202,627.00	253,084.99
Domestic bond fund	5,000,000.00	5,076,599.00
Total investments and cash equivalents	$ 433,812,001.61	$ 465,594,666.01
Less: Cash equivalents	247,583,668.31	
Total investments on the balance sheet	$ 186,228,333.30	

Funds on deposit with trustee of $23,007,797.08 and $23,170,300.77 at June 30, 1996, and June 30, 1995, respectively, in retirement of indebtedness consisted of securities held in the Tennessee State School Bond Authority debt service reserve pool and with First Tennessee Bank.

NOTE 4. ENDOWMENT AND SIMILAR FUNDS AND LIFE INCOME FUNDS

Two categories of university funds are subject to long-term investment: the endowment and similar funds and the life income funds. The investment of these funds is governed by the gift instrument and the investment policies established by the Board of Trustees.

Effective July 1, 1954, the university adopted the policy of investing endowment and similar funds over which it had full investment discretion (and on which the donor or governing gift instrument does not require separate investment) in the Consolidated Investment Pool. This pooling of investments affords closer supervision of the investment portfolio and provides, regardless of size, the advantages of participation in a well-diversified portfolio. All endowment and similar funds not invested as part of the Consolidated Investment Pool are separately invested to observe requirements or limitations imposed by donors. Income earned and distributed on separately invested endowment funds amounted to $385,578.00 for 1996 and $411,742.07 for 1995. Income distributed in accordance with the approved spending plan to endowment and similar funds invested in the Consolidated Investment Pool amounted to $7,884,912.78 for 1996 and $7,347,171.43 for 1995.

Life income funds are separately invested entities requiring detailed accounting to reflect specific compliance with terms of each trust and applicable federal regulations. The investment objectives as reflected in each agreement vary widely since they are affected by the age, income level, and needs of the beneficiaries as well as motives and objectives of the donors. Income realized on these funds for 1996 amounted to $1,750,201.00 and for 1995 amounted to $1,576,809.54.

The book value of endowment and similar funds at June 30, 1996, was $189,344,116.12, and the market value was $234,278,784.26. This compares with the June 30, 1995, book value of $168,514,406.81 and market value of $196,719,677.38. The book value of life income funds at June 30, 1996, was $30,594,330.05, and the market value was $31,978,590.30. The June 30, 1995, book value was $25,435,117.12, and the market value was $26,945,206.49.

NOTE 5. BONDS AND NOTES PAYABLE

Tennessee State School Bond Authority bonds, with interest rates ranging from 3.0% to 7.0%, are due serially to 2022 and are secured by pledges of revenue of facilities to which they relate and certain other revenues and fees of the university, including state appropriations. The total outstanding bonded indebtedness for the university was $184,411,774.79 at June 30, 1996, and $194,635,957.85 at June 30, 1995.

Included in the total outstanding indebtedness is a $242,000 note with the Department of Education which was issued in March 1989. The note carries an interest rate of 3% and is due semi-annually to 2003. The outstanding notes payable at June 30, 1996, and June 30, 1995, were $124,920.41 and $142,082.22, respectively.

Annual maturities subject to mandatory redemption for the next five years ending June 30 are as follows:

1997	$ 10,526,234.60
1998	10,693,335.90
1999	11,099,455.55
2000	11,567,750.69
2001	10,753,628.30
Subsequent Years	129,896,290.16
	$184,536,695.20

Interim and short-term financing for various projects has been secured through the Tennessee State School Bond Authority from the Bond Anticipation Notes (BANs) Program established February 24, 1993, with Prudential Securities, Incorporated, to fund projects under construction. Under the BANs Program, the notes will mature on March 1, 1998, and may bear interest at a variable rate (daily, weekly, monthly, quarterly, semi-annually, annually), or a fixed rate (long-term) determined by the underwriter and remarketing agent, Prudential Securities, Incorporated, for periods selected by the authority. Currently, interest is determined on a weekly basis and payable monthly. The notes are subject to purchase by the remarketing agent on the demand of the holder on any business day pursuant to the conditions established in the Note Resolution as described in the Official Statement relating to the notes. The remarketing agent is to use its best efforts to sell the notes to another holder. If the agent is unable to resell any notes that have been "put," the Standby Note Purchaser is required, subject to certain conditions, to purchase the notes. A standby note purchase agreement with Swiss Bank Corporation, New York Branch, was terminated on June 25, 1996, and a new note purchase agreement was entered into with Union Bank of Switzerland on June 26, 1996. The authority contracted with Union Bank of Switzerland at a rate of .06 of 1% per annum on the available commitment and .05 of 1% per annum on the excess, if any, of $106,173,699 over the available commitment provided that each of the foregoing rates shall each be increased by .10 of 1% per annum effective prospectively to the termination of this agreement. The agreement will terminate on June 25, 1997, unless extended. It is expected that a portion of these notes will be redeemed with the proceeds of the sale of bonds at the end of the construction period for the projects being financed. The terms of the terminated agreement with Swiss Bank Corporation were at a rate of .15% per $1,000 prior to February 24, 1996, and .13% per $1,000 thereafter of the principal and interest commitment of $75,961,644.00; the fee is payable quarterly in arrears. The outstanding balance of the five year notes was $81,251,846.00 at June 30, 1996, and $32,936,846.00 at June 30, 1995. Including the short-term financing, the total indebtedness of the university at June 30, 1996, was $265,788,541.20 and $227,714,886.07 at June 30, 1995.

NOTE 6. OPERATING LEASES

The university has entered into various operating leases for buildings and equipment. It is expected that in the normal course of business such leases will continue to be required. Net expenditures for rentals under leases for the years ended June 30, 1996, and June 30, 1995, amounted to $7,582,225.24 and $7,744,897.42, respectively.

The following is a schedule by years of future minimum rental payments required under noncancelable operating leases that have initial or remaining lease terms of more than one year at June 30, 1996.

Year Ending June 30:	
1997	$ 736,883.44
1998	529,342.68
1999	519,086.00
2000	519,086.00
2001	489,836.00
Later Years	657,288.00
Total Minimum Payments Required	$3,451,522.12

NOTE 7. CAPITAL LEASE OBLIGATIONS

The university has a capital lease agreement which allows the university to purchase a building over a period of years. The university also has capital lease agreements for certain equipment items. Future minimum lease payments under capital leases together with the present value of the net minimum lease payments at June 30, 1996, are:

	Buildings	Equipment	Total
1996-97	$22,246.33	$1,017,672.00	$1,039,918.33
1997-98	-	1,017,101.58	1,015,101.58
1998-99	-	846,158.60	846,158.60
Minimum lease payments	$22,246.33	$2,880,932.18	$2,903,178.51

	Buildings	Equipment	Total
Less amounts representing interest	100.34	238,035.96	238,136.30
Present value of net minimum lease payments	$22,145.99	$2,642,896.22	$2,665,042.21

The total value of the leased building was $3,208,165.70 at June 30, 1996. Two buildings were capitalized under leaseholds payable in the amount of $3,824,165.70 at June 30, 1995. The total value of equipment capitalized under leaseholds payable was $3,607,971.21 at June 30, 1996, and $3,602,722.85 at June 30, 1995.

NOTE 8. INSURANCE-RELATED ACTIVITIES

Risk Management

The university is exposed to various risks of loss related to general liability; automobile liability; professional malpractice; workers' compensation; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters.

a. The university carries commercial insurance for losses related to hired and nonowned automobiles, losses related to railroad protection, and losses related to ten university-owned aircraft. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

b. The state purchases commercial insurance for real property losses above $5 million per year and surety bond coverage on the state's officials and employees. In the past three fiscal years, the state has not had any claims filed with the commercial insurer. A designation for casualty losses in the amount of $5 million has been established in the state's general fund to provide for any property losses other than the commercial insurance coverage. At June 30, 1996, the scheduled coverage for the university was $2,126,090,200 for buildings and $641,143,200 for contents. At June 30, 1995, the scheduled coverage for the university was $1,961,223,200 for buildings and $621,152,200 for contents.

c. The state has set aside assets for claim settlement in an internal service fund, the Claims Award Fund. This fund services all claims for risk of loss to which the state is exposed, including general liability, automobile liability, professional malpractice, and workers' compensation. The university participates in the Claims Award Fund. The fund allocates the cost of providing claims servicing and claims payment by charging a premium to the university based on a percentage of the university's expected loss costs, which include both experience and exposures. This charge considers recent trends in actual claims experience of the state as a whole. An actuarial valuation is performed as of fiscal year-end to determine the fund liability and premium allocation. Since the university participates in the Claims Award Fund, it is subject to the liability limitations under the provisions of the Tennessee Claims Commission Act, *Tennessee Code Annotated*, Section 9-8-101 et seq. Liability for negligence of the university for bodily injury and property damage is limited to $300,000 per person and $1,000,000 per occurrence. The limits of liability under workers' compensation are set forth in *Tennessee Code Annotated*, Section 50-6-101 et seq. Claims are paid through the state's Claims Award Fund. The premium assessed to the university by the Claims Award Fund for the year ended June 30, 1996, was $8,421,538 and for the year ended June 30, 1995, was $1,323,800.

Employee Group Insurance

The state has also set aside assets in the Employee Group Insurance Fund, an internal service fund, to provide a program for health insurance coverage for the employees of the state with the risk retained by the state. All full-time and some part-time university employees are eligible to participate in the Employee Group Insurance Fund. The fund allocates the cost of providing claims servicing and claims payment by charging a premium to the university based on estimates of the ultimate cost of claims that have been reported but not settled and of claims that have been incurred but not reported. Employees and providers have 13 months to file medical claims. The university pays approximately 80% of the cost of insurance, and the employee pays the remaining 20%. All assets, liabilities, and payments are by the state. At June 30, 1996, 13,341 university employees were enrolled in the basic plan or Health Maintenance Organization. At June 30, 1995, 13,684 university employees were enrolled in the basic plan or Health Maintenance Organization.

NOTE 9. RETIREMENT PROGRAMS

The University of Tennessee offers four retirement plans and three deferred compensation plans fully described herewith. All regular full-time employees are required to participate in one of the retirement plans. Regular part-time faculty and staff have the option to participate. Term employees are eligible to join a retirement plan upon completion of six months' continuous service.

Tennessee Consolidated Retirement System

All University of Tennessee regular employees, except those on federal appointments, may participate in a cost-sharing multiple-employer defined benefit plan administered by the Tennessee Consolidated Retirement System (TCRS). The payroll for employees covered by the TCRS plan for the year ended June 30, 1996, was $226,025,636.90 and for the year ended June 30, 1995, was $227,255,746.16. The university's total payroll was $635,095,936.84 for the year ended June 30, 1996, and $627,487,294.16 for the year ended June 30, 1995.

The TCRS provides retirement benefits as well as death and disability benefits. Benefits are determined by a formula using the member's high five-year salary and years of service. Members are eligible to retire at age 60 with five years of service or at any age with 30 years of service. Early retirement with reduced benefits is available to vested members who are at least age 55 or have 25 years of service. Members are vested after five years of service. Death and disability benefits are available to vested members. Disability benefits are available to members with five years of service who become disabled and cannot engage in gainful employment. There is no service requirement for disability that is the result of an accident or injury occurring while the member was performing duties. Benefit provisions are established and amended by state statute. The university is required by state statute, effective July 1, 1981, to contribute the necessary amount to pay benefits when due. Prior to that date, the employee bore a portion of the contribution. Members with contributory service who leave the university are eligible for a refund of their contributions, along with contributions made after July 1, 1981, on the employees' behalf by the university. The university's actuarially required contribution made for the year ended June 30, 1996, was $14,307,283.36, which represented 6.33% of covered payroll. The university's actuarially required contribution made for the year ended June 30, 1995, was $14,399,129.01, which represented 6.34% of covered payroll.

The pension benefit obligation is a standardized disclosure measure of the present value of pension benefits, adjusted for the effects of projected salary increases and step-rate benefits, estimated to be payable in the future as a result of employee service to date. The measure, which is the actuarial present value of credited projected benefits, is intended to help users assess the funding status of the TCRS on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among public employee retirement systems and among employers. The TCRS does not make separate measurements of assets and pension benefit obligations for individual state employers. Therefore, the following information is provided for the entire state employee portion of the TCRS. The pension benefit obligation at June 30, 1996, and at June 30, 1995, determined through an actuarial update performed as of June 30, 1996, was $11,610.6 million and through an actuarial valuation performed as of June 30, 1995, was $10,697.4 million. The net assets, at cost or amortized cost, available for benefits were $12,925.0 million at June 30, 1996, and $11,566.8 million at June 30, 1995, leaving assets in excess of pension benefit obligations of $1,314.4 million at June 30, 1996, and $869.4 million at June 30, 1995. The market value of the net assets available for benefits was $14,100.9 million at June 30, 1996, and $12,552.1 million at June 30, 1995. The university's 1996 and 1995 contributions represented 5.0% and 5.1% of total contributions required of all participating entities.

Ten year historical trend information showing TCRS's progress in accumulating sufficient assets to pay benefits when due is presented in the June 30, 1995, Tennessee Consolidated Retirement System Comprehensive Annual Financial Report.

Optional Retirement Plan (ORP)

The university has three defined contribution plans offered through the Teachers Insurance and Annuity Association-College Retirement Equities Fund (TIAA-CREF), Aetna Life Insurance and Annuity Company, and Variable Annuity Life Insurance Company (VALIC). The plans are available only to eligible faculty and staff exempt from the overtime provision of the Fair Labor Standards Act. In a defined contribution plan, benefits depend solely on amounts contributed to the plan plus investment earnings. State statute requires the university to contribute an amount equal to 10% of the employee's base salary below the social security wage base and 11% above the social security wage base. Members are fully vested upon entry into the plans.

The payroll for employees covered by the defined contributed plans was $292,839,493.63 for the year ended June 30, 1996, and $284,301,905.52 for the year ended June 30, 1995. The university's total payroll was $635,095,936.84 for the year ended June 30, 1996, and $627,487,294.16 for the year ended June 30, 1995. The required contribution made by the university for the year ended June 30, 1996, was $29,529,501.89, which represented 10.1% of the covered payroll, and for the year ended June 30, 1995, was $28,627,971.61, which represented 10.1% of the covered payroll.

Joint Contributory Retirement System - JCRS-A

Employees who were enrolled in the Teachers Insurance and Annuity Association College Retirement Equities Fund (TIAA-CREF) before July 1977 are members of the Joint Contributory Retirement System Plan A (JCRS-A), a defined contribution plan with minimum defined benefits. Enrollment in this plan for new employees has been closed since July 1977.

As in the case of the TCRS and ORP plans, since July 1981, the university pays all retirement premiums for those enrolled in JCRS-A. The primary difference between the JCRS-A plan and the present ORP plan is that JCRS-A members, upon retirement, receive benefits from Aetna, TIAA-CREF, or VALIC and may receive a supplementary benefit from the State of Tennessee. To determine if a JCRS-A member is due a state supplement after retiring, a formula is used which considers years of creditable service and average salary for the highest five consecutive years. JCRS-A members may retire with unreduced formula benefits at age 60 or upon completion of 30 years of creditable service.

The university's contributions, as authorized by *Tennessee Code Annotated*, Section 8-39-301, for JCRS-A members were calculated using the base salary amounts of $75,717,573.19 and $78,687,596.00 for fiscal years 1996 and 1995. The contributions are included in the ORP amounts. University contributions to fund the state supplemental benefit totaled $4,792,754.90 and $4,984,187.94 in fiscal years 1996 and 1995.

Federal Retirement Program

The Federal Retirement Program is a cost-sharing multiple-employer defined benefit retirement program composed of two retirement systems: the Civil Service Retirement System (CSRS) for participants employed prior to January 1, 1984, and the Federal Employees Retirement System (FERS) for participants employed after December 31, 1983. Members vest after various periods of service, the maximum of which is five years. For both systems, benefits are established and contribution requirements are determined by federal statutes.

All regular full-time employees of the University of Tennessee Agricultural Extension Service who hold federal appointments for 51% or more of their time are required to participate in either the CSRS or FERS of the Federal Retirement Program. The payroll for employees covered by Federal Retirement Programs for the year ended June 30, 1996, was $19,878,492.38 and for the year ended June 30, 1995, was $19,986,552.15. The total university contributions in 1996 to the Federal Retirement Program, $1,941,700.14, represented 9.8% of covered payroll. The total university contributions for 1995, $1,908,495.22, represented 9.6% of covered payroll.

Employees who retire under the Civil Service Retirement System will receive annual benefits for life equal to 1.5% of the "high-three" average pay for each service year up to five years, 1.75% of the same "high-three" average pay for each service year between five and ten years, and 2% of the same "high-three" average pay for each service year greater than ten. The "high-three" average pay is the highest pay obtainable by averaging the rates of basic pay in effect during any three consecutive years of service. Participating employees and the university are required to contribute 7% of covered payroll to the plan. Contributions for the year ended June 30, 1996, were $1,779,920.79, which consisted of $907,561.75 from the university and $872,359.04 from the employees. Contributions for the year ended June 30, 1995, were $1,870,281.08, which consisted of $953,544.65 from the university and $916,736.43 from the employees.

Employees who retire under the Federal Employees Retirement System will receive annual benefits for life equal to 1.0% (1.1% if the employee retires at age 62 or later with 20 years' service) of the "high-three" average pay for each year of creditable service (Basic Benefit Plan) plus Social Security benefits, plus an amount from a defined contribution plan (denoted as Thrift Savings Plan, managed by the Federal Retirement Thrift Investment Board). The "high-three" average pay is the highest pay obtainable by averaging the rates of basic pay in effect during any three consecutive years of service. Participating employees are required to contribute .80%, and the university 11.4%, of their salaries to the Basic Benefit Plan. These rates became effective October 1, 1994. In addition, the university is required to contribute 1.0% of each participant's salary to the Thrift Savings Plan plus up to an additional 4% depending upon employees' contributions which can range from 0 to 10% of their salaries. Contributions for the Basic Benefit Plan were $841,226.30 for the year ended June 30, 1996, which consisted of $55,135.25 from employees and $786,091.05 from the university, and $792,057.03 for the year ended June 30, 1995, which consisted of $50,480.50 from employees and $741,576.53 from the university. The contribution requirements for the Thrift Savings Plan were $650,769.34 for the year ended June 30, 1996, which consisted of $402,722.00 from employees and $248,047.34 from the university, and $589,535.86 for the year ended June 30, 1995, which consisted of $376,161.82 from employees and $213,374.04 from the university.

The pension benefit obligation and related disclosure are not available to the university.

Deferred Compensation

The University of Tennessee offers its employees three deferred compensation plans. The university, through the State of Tennessee, provides two plans, one established pursuant to *Internal Revenue Code*, Section 457, and the other pursuant to *Internal Revenue Code*, Section 401(k). The third plan is administered by the university and was established in accordance with *Internal Revenue Code*, Section 403(b). These plans are available to all university employees and permit them to defer a portion of their salaries to future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency. All costs of administering and funding these plans, with the exclusion of $20 monthly university match for the Section 401(k) plan, are the responsibility of plan participants.

Section 457 plan balances have been reported in the State of Tennessee financial statements in an agency fund. All amounts of compensation deferred under this plan, all property and rights purchased with those amounts, and all income attributable to those amounts, property, or rights are (until paid or made available to the employee or other beneficiary) solely the property and rights of the State of Tennessee (without being restricted to the provisions of benefits under the plan), subject only to claims of the state's general creditors. Participants' rights under the plan are equal to those of general creditors of the state in an amount equal to the fair value of the deferred account for each participant. It is the opinion of the state's legal counsel that the state has no liability for losses under the plan but does have the duty of due care that would be required of an ordinary prudent investor. The state believes it is unlikely that it will use these assets to satisfy claims of general creditors in the future.

Since Section 401(k) plan assets remain the property of the contributing employees, they are not presented in the State of Tennessee financial statements. *In-*

ternal Revenue Code Section 401(k) establishes participation, contribution, and withdrawal provisions for the plan. Effective January 1996, the university began providing a $20 monthly Section 401(k) match from unrestricted current funds for employees making a minimum monthly contribution of $20 to the plan. During the year ended June 30, 1996, contributions totaling $3,412,034.46 were made by employees participating in the plan, and a related match of $573,530.00 was made by the university.

In accordance with the *Internal Revenue Code*, employee contributions through the 403(b) plan remain the assets of the employee; therefore, these employee contributions are not reflected in the university's financial statements.

Other Post-Employment Benefits

Health Care

The State of Tennessee administers a group health insurance program which provides post-employment health insurance benefits to eligible university retirees. This benefit is provided by and administered by the State of Tennessee. The university assumes no liability for retiree health care programs. Information on this plan is available at the statewide level in the *Tennessee Comprehensive Annual Financial Report*.

NOTE 10. AFFILIATED ENTITIES

The University of Chattanooga Foundation, Inc., a private nonprofit corporation, maintains an endowment fund of which the University of Tennessee at Chattanooga is the sole income beneficiary. The financial records, investments, and other financial transactions are not managed by the university and accordingly are not included in the financial statements except for certain endowment assets. During the years ended June 30, 1996, and June 30, 1995, the Foundation transferred $2,306,012.00 and $2,854,304.00, respectively, to the university for support of designated projects at the Chattanooga campus. In addition, $167,718.30 and $1,320,936.66 were expended in 1996 and 1995 directly by the Foundation for the benefit of the University of Tennessee at Chattanooga.

Since fiscal year 1985, the Tennessee General Assembly has appropriated $22 million to a Chairs of Excellence Endowment for the University of Tennessee. The appropriations provided that the Chairs of Excellence Endowment be established as an irrevocable trust with the state treasurer and require the university to match the appropriation on a dollar-for-dollar basis. The university has fully matched 47 chairs as of June 30, 1996, and June 30, 1995. The financial statements of the university include as restricted expenditures the amounts expended in the current year to match the state appropriations. The university's balance sheets do not include the amounts held in trust by the state treasurer.

NOTE 11. CONTINGENCIES AND COMMITMENTS

Construction Commitment

The university has contractual obligations for the construction of new buildings and additions to and renovations of existing buildings. The outstanding commitments under such contracts at June 30, 1996, were $39,729,663.80. At June 30, 1995, these commitments were $31,275,948.02. At June 30, 1996, amounts due from or receivable from the state totaled $26,788,768.27 and amounts due from or receivable from the School Bond Authority for capital construction, renovations, and maintenance totaled $7,094,202.64. At June 30, 1995, these amounts totaled $42,899,929.17 and $6,847,632.42.

Construction in Progress

Construction in progress is included in buildings in investment in plant. Forty projects were under construction at June 30, 1996, and 43 were under construction at June 30, 1995. Construction in progress totaled $46,039,884.04 at June 30, 1996, and $69,901,305.59 at June 30, 1995.

Encumbrances

Encumbrances which represent commitments of prior-year funds for goods that have been ordered but not delivered or services that have not been rendered as of June 30, 1996, are recorded as an allocation of the current fund balances. The allocation for encumbrances at June 30, 1996, was $8,728,747.48. The allocation for encumbrances at June 30, 1995, was $9,300,279.62.

Sick Leave

The university's policy is to record the cost of sick leave when paid. Generally, since sick leave (earned one day per month with unlimited accumulation) is paid only when an employee dies or is absent due to illness, or injury, there is no liability for sick leave at June 30, 1996. The amount of unused sick leave at June 30, 1996, was $149,607,387.98 and at June 30, 1995, was $141,239,835.43.

Grants and Contracts

The university receives grants and contracts from various federal and state agencies to fund research and other activities. The costs, both direct and indirect, charged to these grants and contracts are subject to audit and disallowance by the granting agency. The university administration believes that any disallowance or adjustments would not have a material effect on the university's financial position.

Nonvested Equipment

Equipment in the possession of the university valued at $8,167,125.86 and $8,845,824.82 as of June 30, 1996, and June 30, 1995, respectively, is not reflected in the financial statements. This equipment was purchased with restricted grant and contract funds and other funds, and title has not yet been transferred to the university.

Litigation

Various litigation has arisen in the course of conducting university business. The outcome of such litigation is not expected to have a material effect on the financial position of the university.

NOTE 12. PLEDGES

Pledges totaling $30,582,558 restricted to instruction, research, public service, library, operation and maintenance of physical plant, student aid, property, buildings, equipment, endowment, loans, and other restricted purposes, are due to be collected over the next six fiscal years as follows:

Fiscal Year	
1996-97	$ 9,585,179
1997-98	7,028,469
1998-99	4,736,196
1999-2000	5,923,872
2000-01	2,235,474
2001-02	1,073,368
Total	$30,582,558

It is not practicable to estimate the net realizable value of such pledges, and therefore they are not reflected in the accompanying financial statements.